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C O N F I D E N T I A L SECTION 01 OF 04 LAGOS 001531

SIPDIS

STATE PLEASE PASS TO FCC, EX-IM, AND OPIC

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TAGS: ECPS ECON EINV EIND PGOV NI CH
SUBJECT: TELECOM SECTOR GROWS, CHINESE FIRMS EXPAND OPERATIONS

REF: LAGOS 0924

Classified By: Consul General Brian L. Browne for reasons 1.4(b) and (d).

¶1. (C) Summary. Telecom operators believe the Nigerian Communications Commission's (NCC) unified licensing policy allowing existing fixed wireless and mobile licensees to provide both services for voice, data and multimedia will reinforce the current dominance enjoyed by the key players already in mobile telephony. Analysts believe the policy will lead the four major Global System of Communication operators (GSM) to acquire or push most Fixed Wireless (FW) operators from the market. While mobile telephone subscribers has climbed to over 13 million users, challenges such as inadequate power supply, customs clearance delays, multiple taxation, inadequate backbone infrastructure, diesel fuel theft, security and maintenance costs continued to plague the sector. In the meantime, Chinese telecom equipment and service firms Huawei and Zhongxing Telecom (ZTE) are expanding their operations in Nigeria. End Summary.

Background

¶2. (U) The NCC announced February 2005 its plans to introduce a unified licensing regime by February 2006. Under this policy, existing GSM operators (MTN, Vmobile, Globacom, and Mtel) could offer fixed wireless and fixed line services, while FW operators (Starcomms, MTS, Multilinks, and Intercellular) could offer mobile services. FW operators would no longer be confined to specific geographic areas, but could offer services nationwide, putting them in direct competition with the more popular GSM providers (reftel). Operators wanting a unified license would be required to meet conditions specified in the licensing framework which, in theory, was aimed at providing a level playing field for all operators while increasing service penetration.

Unified Licensing Won't Remove GSM Operators Current Dominance

¶3. (C) Economic officers met on September 16 with Vmobile Chief Regulatory Officer J.P Snijders who predicted unified licensing would not change GSM operator behavior. To protect their market from competition, GSM operators would raise the entry barriers so high that potential competitors would be discouraged to invest. According to him, unified licensing was nothing but "political capital" aimed at making the Government of Nigeria appear to be making progress in telecom deregulation. Snijders asserted his company was "following along" simply to appease the NCC. He believed the policy would bring some competition and foresaw the potential for a large South African telecom company or Vodafone vying to obtain a unified license. However, he did not foresee licensing traffic in the opposite direction - relatively small-scale fixed operators entering the GSM market.

¶4. (C) MTN Network Group and Financial Control Manager Olawole Obasunloye stated under the unified license regime, existing GSM operators would remain in the enviable position of shaping the rules of the game. His company would discourage new entrants and would purchase or force out any FW operator posing a threat to MTN's operations in any geographic region. He believed new and existing FW operators could earn profits in regions where GSM operators were not operating, but there was a high likelihood they would be acquired or pushed out by GSM operators. Globacom Marketing and Strategy Director Subhra Das said his company "would not hesitate" to acquire profitable FW operators, and GSM operators "would do everything in their power" to prohibit new entrants from entering the GSM market.

13 Million Subscribers and Rising

¶5. (U) NCC Lagos Zonal Controller Dr. Henry Nkemadu told us

the telecom sector continued to grow. He estimated 13 million active mobile telephone subscribers in Nigeria. Industry experts place the figure higher. MTN claimed over six million subscribers, Vmobile and Globacom respectively claimed about three million each, and Mtel around one million. Snijders, Obasunloye, and Das claimed the number of mobile subscribers increased monthly an average of two to three hundred thousand subscribers per company. Vmobile launched its ROSE (Rolling Out Service Everywhere) initiative to invest USD two billion to expand the number of base stations (currently at 1,500) to 3,000 and increase network capacity to handle ten million active subscribers by 2007.

Fierce Competition, Reduced Revenue

¶6. (SBU) Revenue did not increase in proportion to the increase in the number of subscribers in 2004, operators said. Protracted GSM price wars reduced charges for subscriber identification module (SIM) cards and airtime promotion packages, Obasunloye said. According to him, their SIM card and free 500 minutes of airtime package valued at naira 2000 (USD 15) last year, has been reduced to naira 980 (USD 7), helping to boost subscriber numbers. The cost per minute of GSM airtime during peak hours was reduced from naira 50 (USD .38) to now naira 38 (USD .29), he said. Snijders said some Nigerian consumers had also switched to text messaging costing naira 10 to 15 per minute (USD .08 to .11) as a cheaper alternative to make phone calls. Consumers had also begun "flashing" or developing codes to communicate by dialing and immediately hanging-up before being charged for the call, Snijders said. The reduced cost for airtime, fierce promotion campaigns, and changing consumer behavior led to a diminished rate of return in 2005, operators said. They claimed the average revenue gained per GSM user had been reduced from between USD 30-40 last year to USD 10-23 now. According to Obasunloye, "subscribers are rising, but revenues are not rising as fast as before".

Plenty of Challenges

¶7. (C) Industry experts have complained that infrastructure costs prevented new operators from entering. Unified licensing would not solve this challenge, the experts said. GSM operators rely on Nigeria's National Electric Power Authority (NEPA) for only 16% of their power, spending over naira six billion (USD 45 million) to use and maintain their own generators, including the purchase of 116 million liters of fuel, the NCC said. Vmobile's Snijders said the cost for a base station in Nigeria was three times the cost in Europe; the company spends millions of dollars on maintenance costs for base stations including security, infrastructure, power supply, and logistics. The 35% import duty on telecom equipment and the customs clearance delays also caused "headaches", Snijders said.

Multiple Taxation

¶8. (C) Lack of harmonized tax regime between state and federal governments had led to double taxation on building permits, industry experts said. MTN's Obasunloye stated taxes on masts, towers, building permits, and various environmental tax charges paid to state, federal, and local governments added hundreds of millions of naira in additional costs to GSM operators. Multiple taxation remains a challenge that Snijders felt could only be tackled by a comprehensive tax reform bill.

Inadequate Backbone Infrastructure

¶9. (C) Years of infrastructure neglect by the NCC has meant GSM operators must invest in National Microwave and fiber optic infrastructure in different parts of the country. Chinese firms have been actively bidding in this area. According to Snijders, Huawei Telecom provides GSM radio networks for Vmobile in northern Nigeria, and has been seeking contracts to provide backbone infrastructure for GSM operators across the country. Motorola has been providing backbone infrastructure support mostly in central and southeastern Nigeria, and Ericsson in southwestern Nigeria, Snijders said. The cost of building and operating a 600 km fiber optic backbone is over naira one billion (USD 7.5 million). Industry experts deemed existing backbone infrastructure as inadequate to support the pace of GSM network expansion.

Diesel Fuel Theft

¶10. (SBU) Diesel fuel theft from base stations throughout the country remains a challenge for GSM operators. Obasunloye estimated MTN lost naira four billion (USD 30 million) in costs associated with diesel fuel theft. (Note: This amount seems exaggerated for effect but it does go to show that the GSM operators see this as a serious problem. End Note.) Snijders and Das said diesel fuel theft, and the associated costs, including hiring security guards, building security fences, and securing vehicles cost their companies' millions each year. Vmobile and other companies have tightened security to prevent people from stealing base station equipment in addition to fuel and other supplies.

Chinese Firms Expanded Operations

¶11. (C) Chinese firms Huawei and ZTE have expanded their operations in Nigeria. Obasunloye said Huawei had improved its technology rapidly in the past two years which has allowed MTN to intensify its business operations with Huawei. Huawei now provided 30% of MTN's base stations in contrast to 20% last year, while Ericsson now provided 70%. MTN employees also attended Huawei's USD 7 million training facility in Abuja and Huawei had invested more this year in research and development than 2004. ZTE also had been bidding to provide base stations, Snijders said. Obasunloye said MTN was currently reviewing ZTE's proposals. ZTE had been trying actively to sell its 3G technology, and recently built an assembly-line factory in Abuja to produce and sell phone hand sets.

No Turning Back

¶12. (C) Comment. Despite the costs of doing business in Nigeria, existing GSM operators are bullish, and so are Chinese firms Huawei and ZTE. Industry experts predict active mobile telephone subscribers to exceed 20 million by 2007, placing the potential subscriber base at between 30 and 40 million people in the next five to eight years. Competition in the telecom sector will remain fierce. None of the major GSM operators believe the NCC's unified licensing regime will significantly impact their operations. Even when the unified licensing regime is introduced in February 2006, most observers believe it will take another year before implementation. Given this lag time, GSM operators will continue as they are to spend millions if not billions of naira to build infrastructure and maintain market dominance. Opening the door via the unified licensing policy so companies can do both GSM and fixed wireless services sounds even-handed and competition-enhancing. However, given their size and market share advantage over FW operators, GSM operators might see the new policy as a way to anneal their dominance and actually stifle competition. End Comment.
BROWNE